

EXECUTIVE SUMMARY

The Division of Ratepayer Advocates¹ (DRA) conducted this audit at the request of California Public Utilities Commission (CPUC) President Michael Peevey to “verify what the source of funding has been for PG&E’s recent political activities.”² Pacific Gas and Electric Company (PG&E) spent approximately \$12.6 million on political campaigns opposing the annexation of portions of PG&E’s service territory in Yolo County by the Sacramento Municipal Utility District (SMUD). DRA’s review encompassed PG&E’s activities on four ballot measures: Measure H in Yolo County in the June 2006 elections; and, Measure L in Sacramento County and Measures H and I in Yolo County in the November 2006 elections.

This audit addresses two basic questions:

1. Are PG&E’s campaign expenditures considered utility expenses that may be recovered from its customers? If not, how will the CPUC ensure that the expenditures are not recovered in rates?
2. How has PG&E funded its campaign to defeat the Yolo annexation ballot measures, including the bill insert and customer service message?

In answer to the first question, based on a review of the CPUC proceedings that determine the amount of revenue PG&E may collect in rates from its customers covering a period from 2000 through 2011, DRA concludes that:

¹ DRA is an independent division within the CPUC and is statutorily mandated to advocate for and represent the interest of customers of regulated public utilities with a goal to obtain the lowest possible rates for service consistent with safe and reliable service levels.

² Letter dated Nov. 9, 2006 from President Peevey to Senator Christine Kehoe and Assembly member Lloyd Levine.

- PG&E's campaign expenditures are not utility expenses that may be recovered from its customers in rates.
- DRA's upcoming review of PG&E's costs and expenses in the normal CPUC General Rate Case process will ensure that unauthorized expenditures are not recovered from customers in the future. DRA will apply heightened vigilance to ensure that PG&E's campaign expenditures will not be recovered in future rates.

Answering the second question, of how PG&E funded its campaign to defeat the Yolo annexation ballot measures, DRA's investigative audit of PG&E books and records revealed the following:

- PG&E incorporated a legal entity, The Coalition for Reliable and Affordable Electricity (CRAE), and fully funded it using shareholder money to oppose the annexation of its Yolo territory. To that end, CRAE funded the bulk of campaign activities at a cost of \$11.5 million.
- PG&E incurred other expenses, including approximately \$700,000 of Internal Costs for: employee time, internal labor and related expenses, postage for a campaign-related bill insert, use of PG&E's West Sacramento Office, use of call centers; and, approximately \$400,000 of Outside Costs paid by PG&E to vendors and contractors. All of these expenses were reviewed and traced to shareholder funded accounts.

As a result of this audit, DRA concludes that the \$12.6 million expended by PG&E to defeat the annexation of its Yolo territory was properly recorded in accounts funded by PG&E shareholders, and not charged to accounts funded by PG&E ratepayers. However, DRA does believe that there are areas in which PG&E could improve its record keeping and accounting of similar types of activities in the future. Accordingly, DRA makes the following recommendations:

- **Recommendation 1: Employee time and expenditures spent on campaign activities should be tracked using the time reporting system agreed to by DRA and PG&E in the settlement adopted in CPUC Decision 07-03-044, which requires written tracking on a daily basis. In addition, employees who are not covered by that agreement should also be required to track their time in writing on a daily basis when they spend time on political campaigns.**

- **Recommendation 2:** For future political campaign efforts, costs for the use of existing Utility Facilities, such as call centers, offices and monthly bills, should be allocated to shareholders based on the full fixed and incremental costs of those facilities, rather than just the incremental costs as was done by PG&E. Alternatively, these costs could be treated the same as utility affiliate costs, or at a minimum shared 50-50 between shareholders and ratepayers.
- **Recommendation 3:** Establish a one-way tracking account that would require that the costs allocated to the utility shareholders are credited back to ratepayers regardless of whether or not these credits appear in the Historic Data for setting future rates in the utility's next rate case.
- **Recommendation 4:** For future political campaign efforts, all Outside Costs should be paid for using a separate entity such as CRAE, rather than being paid directly by PG&E, to provide greater clarity on the sources and uses of funds expended on campaigns.